CRITIQUE OF
RESOURCES COMMITTEE REPUBLICAN ENERGY BILL
(April 7, 2003)

The Resources Committee Republican Energy Bill is premised on a 'drill at taxpayer expense' approach to the management of energy resources on public lands. At the same time that the bill lessens environmental protections, including allowing the development of the Arctic National Wildlife Refuge, it does little to meaningfully enhance America's energy security and instead increases federal and state subsidies of energy development without regard to whether such incentives are actually needed or beneficial to the public in the long-term.

OIL AND GAS DEVELOPMENT

The oil and gas development provisions of the Resources Committee Republican Energy Bill are a buffet line of the oil and gas industry's preferences for use of the public lands, with energy development reigning supreme and its costs being minimized at taxpayers' expense.

According to the Congressional Budget Office, similar energy legislation reported by the Resources Committee in 2001 (H.R. 2436) would have increased direct spending by a net $215 million over the next decade and in addition, would have cost a net $136 million to implement during the 2002-2006 period , assuming appropriation of the necessary amounts. The costs of the oil and gas provisions were not fully offset in the bill, even assuming projected ANWR revenues.

This year's package is even more generous to the oil and gas industry, as "royalty relief" has been enhanced for deep water leases in the Gulf of Mexico, applied to "marginal wells," and new provisions added for deep drilling on previously issued "shallow" water leases in the Gulf and for future leases in the Alaska OCS. Other costly provisions include a mandate to grant to oil and gas industry royalty credits for the costs for environmental (NEPA) analysis of proposed drilling projects. CBO's analysis of the impacts of the new bill on the federal budgets will not be available at the time of the markup.

Royalties in Kind: Provisions of the bill would make permanent the Secretary's authority to take federal royalties "in-kind." In the face of mounting evidence that suggests taking royalties in kind instead of in cash payments actually costs the government revenues, the bill would permanently authorize the Secretary to market, process and transport oil and gas taken in-kind. The Minerals Management Service (MMS) would then market the products in order to recoup a royalty. However, according to the GAO's most recent findings, after five years of conducting pilot programs and completing 24 oil and gas pilot sales, the MMS cannot: monitor or evaluate its RIK Program, determine the program's overall cost and effectiveness, nor ascertain whether RIK generates *at least as much* revenue as traditional cash royalty payments as required by law.

This is problematic in light of the Majority's intention to make the RIK program permanent. According to GAO: "MMS will be unable to determine whether RIK sales generate more or less revenue than traditional cash royalty payments; whether MMS obtains fair market value; and hence, whether it should convert the RIK pilots to an operational status."

Oil and Gas Resource Assessment: The bill would authorize Interior to revamp its recent study of oil and gas resources on public lands to evaluate alleged impediments to development, such as permit delays. This section stems from a January 2003 Bush Administration study which found that only 15 percent of "technically recoverable" oil and 12 percent of natural gas reserves from federal lands are unavailable for development. Faced with losing credibility in continuing to make the public relations pitch argument that too many federal lands are closed to oil and gas development, industry now alleges that the Interior report was flawed because it did not address post-lease impediments, such as compliance with environmental laws and wildlife stipulations.

Royalty Holidays: The bill would require the federal government to provide generous 'royalty holidays' to all federal oil and gas leases in the deepwaters of the Gulf of Mexico, shallow waters of the Gulf where deep gas wells are being developed and offshore Alaska.

By waiving federal royalty collections on huge amounts of publicly-owned oil and gas the bill constitutes a significant taxpayer subsidy – at a time of high prices and record profits – for the oil and gas industry. The 'royalty relief" provided in the bill is *more* generous than that authorized by Congress in the OCS Deep Water Royalty Relief Act in 1995. The controversial 1995 Act was justified at the time by its proponents on the basis of countering *low* oil and gas prices and the need to encourage emerging technology in frontier deep water areas of the OCS. Neither rationale exists in 2003 since prices are high and technology has evolved so that operating in water deeper than 200 meters is commonplace. There is no evidence that major oil companies will abandon promising areas in the Gulf of Mexico or Alaska absent additional "royalty relief" in new lease sales.

Ironically, George W. Bush attacked Vice-President Gore for supporting "royalty relief" for deep water OCS drillers during the 2000 campaign, criticizing it as "giving major oil companies a huge tax break."

According to last year's CBO estimate on a far less generous royalty holiday: "But since industry discounts the value of future profits, an overall loss of receipts would occur over the life of the lease as higher initial bonus bids would not fully offset foregone royalty receipts." CBO estimated that the deepwater royalty holiday alone would reduce offsetting receipts by about $91 million over the 2002-2011 decade. Further, royalty losses would continue over the life of the leases, according to CBO. At the markup, Rep. Tauzin offered an amendment, which was adopted, that will substantially increase the cost of the shallow water/deep gas well provision.

Royalty Relief for Marginal Properties: The bill also would provide royalty relief to marginal wells and as CBO noted in 2001: "[the provision] does not specify how much royalty relief would be provided, or how long such relief would last." CBO estimated that the provision would reduce royalties by about $491 million over the next ten years---with $242 million from offshore leases and $249 from onshore leases. Western States that share equally in the onshore receipts would lose $121 million during the same time period.

Impediments to Energy Development on Federal lands: As in the 2001 bill, the current legislation would require the federal government to conduct an internal review of existing oil and gas leasing procedures in order to find ways to facilitate and streamline energy development. For instance, provisions of the bill would require the Interior Secretary to ensure timely action on oil and gas leasing decisions by expediting NEPA compliance and requires the Interior and Agriculture Departments to enter into an inter-agency agreement to ensure timely processing of oil and gas leasing decisions. Taken together, these provisions would significantly diminish conservation measures on public lands for water resources, wildlife and fish habitat and scenic landscapes. The effect of these provisions would be to elevate energy production on public lands to a dominant use, and was opposed in the last energy package by groups including the National Rifle Association, Trout Unlimited, the Izaak Walton League and other sporting and fishing groups.

Oil and Gas Monopolies: The bill would also lift the limitation on the number of public land acres an oil company can hold in any one State. The Mineral Leasing Act of 1920 restricts the interests a company can own in federal oil and gas leases in any one State to 246,080 acres. Historically, the acreage limitation in the Mineral Leasing Act responded to public concern over a few major integrated oil companies locking up potential supplies of crude oil from federal lands in the West. As originally enacted, the Act forbade any person from owning more than three federal oil and gas leases in any state and more than one lease in an oil and gas field. Industry asserts, that under present-day conditions increased acreage and more time are necessary to protect the huge investments now needed to maintain rates of discovery. However, under existing law, and with the cooperation of the Department of the Interior, companies are able to administratively exempt federal acreage from the 246,080-acre limit per state either through unitization or by the creation of a development contract. Although the BLM has been cooperative in working with companies that find they are bumping up to or exceeding the acreage cap, industry is advocating that Congress remove acreage limitations.

Orphaned Well Reimbursement: This year's bill contains a provision requiring the federal government to reimburse oil companies that reclaim orphaned oil and gas wells. It is unclear why the taxpayer should foot the entire bill for the oil and gas industry cleaning up their own misdeeds. Further, the bill provides that a credit of 100% for onshore and 115% for offshore reclamation may be taken against any federal lease which will reduce not only federal revenues but state revenues in those states where the lease is located.

NEPA Reimbursement: As in last year's energy bill, this title would authorize the reimbursement of non-federal NEPA costs through royalty credits. Current law requires the Interior Department to complete all analyses required under NEPA to proceed with mineral leasing and development of federal lands. Because funding levels typically fall short of the amounts needed to complete this work, lessees are allowed to pay for third-party consultants to complete the required work on behalf of Interior. The bill, however, would require the federal government to reimburse oil and gas lessees, through credits against future royalty payments, for the costs to the lessee of completing required NEPA work. Last Congress, the CBO estimated that these provisions would cost $370 million over the 2002-2011 period. Further, of the $370 million lost, Western States that receive half of the revenues from onshore leases would lose $185 million (half of the $370 million total).

OCS Moratoria Areas. As an initial step towards lifting the moratoria on oil and gas leasing off the coasts of States such as California, Florida, North Carolina, New Jersey and Massachusetts, the bill would require a comprehensive inventory of OCS oil and gas resources---including resources located in moratoria areas. The bill would require a computation of the estimated amounts of oil and gas resources in moratoria areas; an analysis of how estimates for such resources have changed over time; and how limitations to development affect domestic supply and how understated inventories affect domestic energy investments. The section would also require a study of the occurrence and distribution of methane hydrates.

West Delta Payback. Finally, the bill would obligate the federal government to pay the State of Louisiana approximately $35 million through credit on payment of future Federal offshore royalties in order to satisfy the State's assertion that it is owed these monies due to oil and gas drainage in the West Delta Field off the coast of Louisiana despite numerous court decisions to the contrary.

From 1986 through 1999, Louisiana received approximately $867 million in revenues from activities associated with 8(g) zone leases, including $8 million in revenues specifically associated with the West Delta leases. The Administration has consistently opposed this provision on the grounds that the so-called 8(g) payments have already repaid the State for any losses. Further, the Administration has consistently disputed the State's calculation of its claim.

ARCTIC NATIONAL WILDLIFE REFUGE DEVELOPMENT

The bill would repeal the oil and gas leasing ban established by Congress in Section 1003 of the Alaska National Interest Lands Act of 1980 and opens 1,549,000 acres of the Arctic National Wildlife Refuge to leasing, exploration and potential development. The Clinton Administration opposed leasing in ANWR and the Department of the Interior in the past has described this 1.5 million acre area – the coastal plain -- as the "biological heart" of the Arctic Refuge. On March 12, 2003, Interior Secretary Norton testified before the committee on behalf of the Bush Administration in support of oil development in ANWR and described the coastal plain as "an area of flat, white nothingness."

The Arctic Refuge was first protected as an internationally important wildlife conservation area by the Eisenhower Administration over four decades ago in 1960 and designated a 19.6 million acre national wildlife refuge by Congress in 1980.

The Arctic Refuge is the only area on the North Slope of Alaska that has been set-aside by Congress as off-limits to oil and gas leasing. Areas currently open to leasing include state-owned lands at Prudhoe Bay, private lands held by the Arctic Slope Regional Corporation, and public lands in the 23 million acre National Petroleum Reserve-Alaska (NPR-A) and the OCS. In the wake of the Clinton Administration leasing selected areas in the northeast portion of NPR-A, the Interior Department is currently planning to lease up to *nine million additional* acres in NPR-A and to conduct offshore OCS lease sales as well.

The bill would authorize oil gas leasing in the Arctic Refuge under broad exemptions from environmental laws. For example, provisions of the bill would exempt oil and gas leasing in the Arctic Refuge from the National Wildlife System Administration Act of 1996's requirements that such activities be determined to be "compatible" with the conservation purposes of the refuge. Provisions of the bill would deem that an EIS prepared by the Reagan Administration -- 16 years ago in 1987 -- satisfies NEPA and waives any further "no-action" analysis. The bill would also arbitrarily restrict the ability of the Fish and Wildlife Service to manage caribou calving and other sensitive areas by setting a limit of 49,000 acres -- only 3 percent of the 1.5 million acre coastal plain – which may be administratively protected from development.

In addition, under the terms of the Alaska Statehood Act of 1958, *ninety percent* of any revenues from Arctic Refuge oil and gas leasing would go to the State of Alaska. However, the bill would alter that revenue split to 50/50 between the State of Alaska and the Federal government. This unilateral change in the terms of Alaska's admission to the Union by Congress will likely invite a legal challenge by the State of Alaska to obtain 90 percent of the revenue.

Further undermining potential Federal revenues, the bill -- in order to "remove clouds on title" -- conveys additional surface land rights within the ANWR coastal plain to the Kaktovik Inupiat Corporation (KIC) and subsurface to the Arctic Slope Regional Corporation (ASRC). Both corporations *already* own 92,000 acres of lands within the coastal plain area by virtue of a controversial 1983 land exchange executed by Interior Secretary James Watt

Proponents of ANWR development have often cited USGS "high-end" estimates of up to 16 billion barrels of "technically" recoverable oil available on the coastal plain. In scoring the Bush Administration's FY 04 budget, however, CBO used USGS estimates to conclude that 2.5 billion barrels of oil would be economic to produce. Even if oil were to be discovered in economic quantities, the lag time to bring Arctic Refuge oil to market (including expensive construction of production and delivery system infrastructure) would take more than a decade. Accordingly, CBO does not score any royalty (production) revenues within the next ten years.

FEDERAL COAL LEASING

Essentially a wish list of the Western coal mining industry, provisions of the bill would significantly dilute the competitive nature of the federal coal leasing program, allowing a few large coal companies to control a growing amount of America's coal resources to the detriment of electricity consumers and coal producers in other States.

In general, under the bill, provisions of law which require that certain federal coal resources be made available on a competitive basis would be eliminated. The bill would also undermine requirements for the diligent development of federal coal leases, allowing them to be held indefinitely. The net effect is that if enacted into law these provisions would place the vast majority of federal coal resources in the Powder River Basin of Wyoming into the hands of one or two companies. In effect, a monopoly that could lead to pricing practices to the detriment of the consumer.

As it stands, electric utility companies have filed with the Surface Transportation Board seven cases challenging the reasonableness of coal rates involving Powder River Basin coal. These utility companies–Northern States Power, Public Service Co. of Colorado, West Texas Utilities Co., Texas Municipal Power Agency, Wisconsin Power & Light Co., Ottertail Power Co., and PPL Montana–are alleging that market dominance exists and that the delivered price of Powder River Basin coal is unreasonable. These utilities are looking out for their customers, because as it stands, the cost of fuel is normally transferred by the utility directly to the consumer. The bill would add insult to injury by reducing competition in the actual production of coal from federal leases in the Powder River Basin.

These are not, by any means, the only utility companies which purchase Powder River Basin coal. Whether it be Arizona Public Service Co., Cajun Electric Power Coop, Central Power & Light of Texas, Dairyland Power Coop in Wisconsin, Detroit Edison, Nebraska Public Power, Oklahoma Gas & Electric, Public Service Co. of Colorado–their consumers stand to lose with the creation of a monopoly in their supplier of coal.

Specifically, the bill would repeal the existing 160-acre limitation for lease modifications. In Wyoming's Powder River Basin, where there has been fierce competition between Arch Minerals and Kennecott Energy to secure leases for the remaining unleased acreage, a coal company seeking to expand its operation would submit a plan modification for additional acreage and not have to compete for the coal as is currently the case. By eliminating competition for the coal, the bill would foreclose the kind of increased bonus payments secured by the BLM in recent years. A 2002 Powder River Basin lease sale generated a $328 million bonus payment from Kennecott. Had this title been in effect at that time, the State of Wyoming would not have received its approximate $164 million share of the bonus payment.

While instilling a level of competition into the federal leasing program in 1976, Congress also took care to instill a "system of deferred bonus payments" in the leasing program to facilitate payment of this business expense by the coal lessees. Under the deferred bonus program, BLM gives the successful coal lessee the option of paying the bonus payment in full at the time of lease issuance or in five equally divided payments over five successive years. The BLM requirement to secure a bond, or other financial guarantee, in the amount due to the U.S. Treasury is simply good business practice.

The bill, on the other hand, would not only eliminate the generation of bonus payments (by eliminating the 160-acre modification limit and thus foreclosing competitive leasing), but in those instances where competitive leasing is or has been held the bill would encourage and enable coal companies to terminate a federal lease and walk away scot-free without paying any remaining balance on any outstanding deferred bonus payments.

Not only will the federal government and taxpayer lose under this title of the bill, mineral leasing states, such as Wyoming or New Mexico, will also see a reduction in their share of revenues generated from coal leasing when deferred bonus payments are not paid in full.

In addition, the bill would further degrade the competitive leasing program as follows:

It would allow coal companies which hold large amounts of acreage under federal coal leases that have been consolidated into "logical mining units" (LMU) for periods exceeding 40 years. Current law requires that when a coal company creates an LMU, the combined acreage must be entirely mined out within 40 years.

The bill would allow coal operators to hold LMU's for longer than 40-years even though there is no record or indication that this is necessary. During a February 27th hearing in the Senate Energy and Natural Resources Committee, Steven Lear, President of Arch Minerals testified that the change would, "allow long term efficiency and orderly development of federal, state and private coal and minimize the potential for bypassing nearby coal resources…" However, he did not identify any mines that are in need of this adjustment, nor why allowing the coal industry to hold large areas for longer than 40 years would be in the public interest. .

The bill would also change the formula for advance royalties. Advance royalties are payments made under a federal lease in advance of actual production which are required when an operation wants to maintain its lease even when it is not producing coal (as required by the lease). Currently, BLM calculates advance royalties as equal to no less than the production royalty that would otherwise have been paid taking into account a fixed reserve to production ratio. The bill would change that formula to one that reflects "spot markets." According to BLM officials, for many parts of the country, e.g., States of Washington, Colorado, Kentucky, there are no reliable spot markets for the particular type of coal produced there.

Finally, while current law prevents the Secretary from excusing a coal company from its legal obligation to pay advance royalties, the bill would enable the Secretary to forgive a coal company's financial obligations when such company opts to stop producing coal for an unspecified period of time.